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The Director of Central Intelligence
Washington, D.C. 20505

NIC # 06900-84
10 December 1984

National Intelligence Council

MEMORANDUM FOR: Director of Central Intelligence
Deputy Director of Central Intelligence

FROM: [redacted] NIO/Economics
NIO/East Asia

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SUBJECT: US-Japan Trade Discussions at the
11 December Cabinet Meeting

1. The Cabinet will discuss new strategies for dealing with the US-Japan trade problem at its 11 December meeting.
2. An options paper prepared for the Trade Policy Committee by an interdepartmental team headed by USTR suggests that the President make a new demarche at his 2 January meeting in California with Prime Minister Nakasone aimed at obtaining a commitment from Japan to halve its bilateral trade deficit with the United States and double Japanese imports of manufactures over a two-year period. It also suggests taking strong retaliatory action should Japan not be forthcoming in negotiating expanded access to selected sectors of the Japanese market. The options presented will not have a significant near-term impact on US-Japan trade.

3. The attached talking points cover the timing of the demarche, Nakasone's ability to follow through, and the possible impact on our relationship of an increased level of confrontation over these issues. Attached papers for your background include:

- A summary of the Trade Policy Committee Paper.
- A comparison of the proposed initiative with a similar initiative taken in 1977/78.

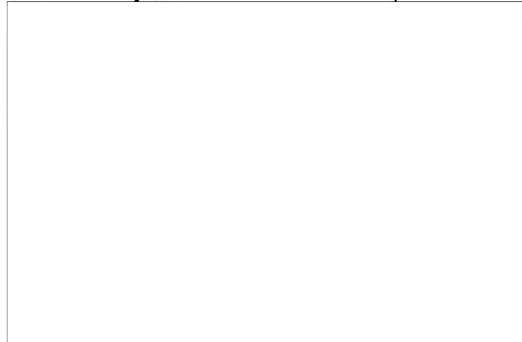
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- An analysis of Nakasone's handling of bilateral issues to date.
- A summary of two-way trade by sector.



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**Attachments,
As stated**

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Summary of The Trade Policy Committee Paper

The Problem

The TPC paper notes that despite four years of negotiations and five trade packages, our trade problems with Japan continue and, indeed, increase.

- Japan is in the throes of a classic export-led growth spurt with exports up 16 percent year over year, accounting for half of Japan's growth last year.
- Manufactured imports still account for only a small amount; \$267 per capita, 2.8 percent of GNP, levels far below those for other developed countries.
- Tokyo is still following a policy of "national autonomy" in sectors where the US is competitive--satellites, telecommunications, software, etc.
- Absent some sort of corrective action, according to an Industrial Bank of Japan report, Japan's global surplus on trade in goods and services could reach a cumulative \$400 billion from 1983-1990, thus rivaling the OPEC surplus of 1974-1981.

Recommendations

The paper recommends that, beginning with President Reagan's meeting with Prime Minister Nakasone in California on 2 January, the US launch a two-pronged attack aimed at increasing Japan's imports of manufactures from the rest of the world.

- The US would initiate intensive discussions to remove trade barriers in selective sectors--the "Market Oriented, Selective-Sector Option" (MOSS) approach formulated by Treasury.
- Teams headed by sub-cabinet officers would negotiate on these sectors, setting targets and following up on agreements.
- The second prong involves setting targets for manufactured imports overall, establishing objectives and follow-up discussions.
- The goal is for Japan to halve its bilateral trade deficit with the United States and double imports of manufactures in two years.
- Lastly, the paper suggests retaliatory action using the President's authority in areas where the Japanese are taking unjustifiable action--policies on standards are recommended as a possible starting point.

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Comparison with 1977-78 US Demarche

The Japanese have successfully "managed" a similar US demarche in the past.

- In the late 1970s, targets were established for increases in manufactured imports and a specific industry, the NTT-led telecommunications sector, was set up as a special beachhead.
- The Japanese were able to fend off these initiatives with buying missions, early tariff reductions, purchase of such non-high-tech goods as telephone poles for NTT, and a series of excuses for why their performance could not reach target levels.
- These discussions and the follow-up were conducted at the sub-cabinet level and were coordinated by the STR.
- As to retaliation, the Japanese sensed correctly that, despite threats by the Administration, there was not a Congressional consensus for strong retaliatory action; Presidential authority to come down hard on key sectors was not used.

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JAPAN: NAKASONE ADMINISTRATION'S HANDLING OF ECONOMIC ISSUES OF CONCERN TO UNITED STATES

<u>Issue</u>	<u>Status*</u>	<u>Comments</u>
Foreign direct investment in Japan	●	In May 1984 Diet revoked regulations limiting foreign investment in 12 Japanese companies. Improvements also made in approval process for direct investments.
Financial liberalization		Much progress made in implementing May 1984 yen/dollar accord, which promotes deregulation. Differences over trust banking and Euroyen markets remain.
Whaling moratorium		Tokyo signed agreement in November 1984 to end sperm whaling as of 1988, but disagreements with Washington over interpretation have subsequently arisen.
Agricultural quotas and tariffs		Agreement reached in spring 1984 calls for expansion of beef and citrus imports over next three years. Government refuses, however, to consider complete liberalization of agricultural imports.
Standards and certification procedures		Recently have begun to accept foreign test data but implementation in several key areas still slow.
Purchase of foreign satellites		Tokyo will allow private firms to purchase foreign satellites, but government policy of domestic development of satellites remains firm.
Removal of semiconductor tariffs	●	Elimination of tariffs approved by Tokyo and will be enacted when parallel legislation passed by US Congress.
Permission for foreign lawyers to practice in Japan	●	No movement so far and none likely before 1987.
Energy purchases from United States	●	Participating in feasibility study of Alaskan LNG pipeline but dragging feet on boosting coal purchases.
Sales of foreign cigarettes		Japan Salt and Tobacco Company monopoly on sales ended, but US companies' concerns about distribution system persist.
Software legislation		Proposed protectionist legislation stalled by bureaucratic wrangling but not yet dead.

Telecommunications legislation	Foreigners will be allowed to sell value-added networks after Nippon Telegraph and Telephone (NTT) privatized in April 1985. New equipment standards being drafted--appears they may be more restrictive than before.
Excise taxes	Expanding number of items subject to excise taxes, which hit import sales disproportionately.
Policies concerning depressed industries	Still permits depressed industries to form cartels, limiting foreigners' sales opportunities. Continues to restrict foreign access to industrial trade councils.
NTT procurement of foreign telecommunications equipment	After bilateral agreement took effect in 1980, foreign sales to NTT increased initially, but US sales have declined recently. Outlook uncertain after return of NTT to private sector.
Restraint on steel shipments to United States	Have expressed willingness to accept export restraints although have yet to agree on limits for various types of steel.
Voluntary restraint on exports of cars to United States	Decided to extend initial agreement signed in 1980 for a fourth year. Bureaucrats have hinted extension in 1985 also possible.

LEGEND*

- indicates that issue basically resolved during Nakasone's tenure.
- indicates that progress has been made but problem areas remain.
- indicates that no real movement has occurred since Nakasone assumed office in 1982.

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JAPAN-UNITED STATES: BILATERAL TRADE DATA

	<u>U.S. Exports to</u> <u>Japan, 1983</u>	<u>Percent</u> <u>of Total</u>	<u>Japanese Exports to</u> <u>United States, 1983</u>	<u>Percent</u> <u>of Total</u>
	<u>Value</u> <u>(\$ Billion)</u>	<u>Exports</u>	<u>Value</u> <u>(\$ Billion)</u>	<u>Exports</u>
Total	21.6	10.8	43.3	29.5
Food	6.0	17.2	0.3	21.5
Soybeans	1.2	19.5	Negl.	34.7
Corn	1.8	27.2	Negl.	Negl.
Wheat	0.6	9.4	Negl.	Negl.
Meat	0.6	38.2	Negl.	11.7
Fish	0.5	53.8	0.2	29.8
Raw Materials	3.3	24.8	0.1	7.1
Wood	0.9	42.5	Negl.	0.3
Cotton	0.5	27.2	Negl.	0.4
Fuels	2.1	21.4	Negl.	3.6
Coal	1.0	24.3	Negl.	2.2
Petroleum Products	0.7	15.3	Negl.	4.6
Manufactures	10.0	7.4	42.3	29.9
Medicine	0.5	20.3	0.1	29.5
Computers	0.5	10.8	2.0	53.6
Office Machines	0.5	8.3	0.7	49.6
Aircraft	1.3	10.9	0.1	65.9
Chemical Elements	1.3	15.9	0.5	17.7
Trucks	Negl.	0.6	1.9	29.7
Cars	Negl.	0.9	10.9	55.8
Motorcycles	Negl.	9.9	1.0	47.1
Car Engines	0.1	2.3	0.7	30.0
Machine Tools	Negl.	7.1	0.5	32.1
Scientific Equipment	0.7	10.1	1.0	30.5
Electrical Machinery, which includes Telecommunications	0.9 0.2	5.9 5.9	4.4 1.9	28.7 40.5